Petition

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NO: _____

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

IN THE MATTER OF NATIONAL
HOSPITAL AND INSTITUTIONAL
BUILDERS CO.

PHILIP GOLDSTEIN, NEW YORK CITY
DEPARTMENT OF BUILDINGS and NEW YORK
CITY BOARD OF STANDARDS AND APPEALS,

Petitioners,

v.

JAMES L. GARRITY, Trustee of Debtor,

Respondent.

PETITION FOR A WRIT OF CERTIORARI
FROM AN ORDER OF THE UNITED STATES
COURT OF APPEALS FOR THE SECOND
CIRCUIT.

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QUESTIONS PRESENTED

1. Whether a bankruptcy court has subject matter jurisdiction to enjoin enforcement of police and regulatory powers of a governmental agency on any grounds?

2. Whether the automatic stay of Bankruptcy Rule 12-43 applies to bar enforcement of police and regulatory powers?

3. Whether a certificate of occupancy is "property" of the debtor within the constructive custody of the bankruptcy court?

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* * * *

STATEMENT

The petitioners, Philip Goldstein (the Borough Superintendent of Staten Island of the New York City Department of Buildings), the New York City Department of Buildings, and the New York City Board of Standards and Appeals,*

* The New York City Board of Standards and Appeals (BSA) is a local quasi-judicial tribunal with jurisdiction, inter alia, to determine whether the zoning regulations have been violated and is authorized to revoke a certificate of occupancy if it finds that a building cannot legally be used for the purpose set forth in the certificate (N.Y. City Charter Sec. 645(b)(3)(e)). BSA has yet to consider any of the zoning issues mentioned herein by reason of the injunction.

seek a writ of certiorari to review an order of the United States Court of Appeals for the Second Circuit entered on August 17, 1981; no motion for rehearing was filed.

The Second Circuit, by a divided panel, reversed an order of the United States District Court that dissolved a Bankruptcy Court injunction barring the Department of Buildings from proceeding with its application before the Board of Standards and Appeals to revoke a Certificate of Occupancy for use of a facility owned by the Debtor as a nursing home. The Second Circuit held that the Bankruptcy Court had jurisdiction to enjoin the City from enforcing its zoning laws, but that such jurisdiction should be exercised only if a

finding of "bad faith" enforcement is made by the court, and remanded the case to the District Court to determine the issue of bad faith. Pending such determination, petitioners have been enjoined from enforcing applicable laws. The opinion of the Circuit Court below conflicts with this Court's rationale in Palmer v. Massachusetts, 308 U.S. 79 (1939), and with decisions of the Third, Sixth, Seventh, Eighth and Ninth Circuits.*

*See cases cited on pages 26-27, 32 infra.

OPINIONS BELOW

On August 17, 1981, the United States Court of Appeals for the Second Circuit filed an order and opinion (as yet unreported) reversing the order of United States District Judge LEVAL which reversed an injunction order issued by Bankruptcy Judge GALGAY, permanently enjoining the City from taking any action to revoke a certificate of occupancy issued in 1973 to use a certain facility owned by the Debtor as a nursing home.

The Circuit Court's Opinion was published at 658 F.2d. 39 and is reproduced at Appendix A. The Opinion of the District Court was published in 9 B.R. (West's) 948, and is reproduced at Appendix B. The Opinion of the Bankruptcy Court is reproduced at Appendix C.

JURISDICTIONAL STATEMENT

The judgment of the Court of Appeals was entered on August 17, 1981. Title 28 U.S.C. §1254(1) authorizes this Court to review cases in the courts of appeal "by a writ of certiorari upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree."

STATEMENT OF THE CASE

(1)

Debtor's sole asset is a parcel of real property located at 1000 Targee Street, Staten Island, New York, which is improved by a structure built to be used as a nursing home. The home was built by an affiliated predecessor in title from 1969 to 1973, pursuant to approval of State and City health authorities. Construction of a nursing home at that time did not require a variance or special permit under the then-existing zoning laws of the City of New York.

Upon completion of construction in 1973, a final Certificate of Occupancy (C.O.) was issued by the City Department of Buildings, which certificate evidenced that the building met building code requirements and that the use thereof as a nursing home was legal at the time.

The nursing home was never opened because the New York State Public Health Council declined to give the home "establishment approval" due to an excess of nursing homes in Staten Island.

In early 1974, the City amended its Zoning Resolution to prohibit construction of nursing homes in certain designated residential areas, including the area of Staten Island in which 1000 Targee Street is located, without first obtaining a Special Permit from the City Planning Commission. Special Permits are not granted as a matter of right, but may be granted only if the proposed development meets certain stated standards. The permit may also be conditioned upon provision of appropriate safeguards, such as off-street parking and related improvements, which the City Planning Commission finds will minimize the adverse impact

of the development on the character of the surrounding area.

Under the Zoning Resolution, an amendment barring use of a facility already in existence renders such facility a nonconforming use, which use may nevertheless legally continue to operate for so long as the structure exists and the use is uninterrupted. If, however, a legal nonconforming use is discontinued for two years or more, it is deemed abandoned and may no longer be lawfully used for such nonconforming purpose, irrespective of the existence of a valid C.O. (See, Zoning Resolution, §§ 12-10, 52-61, pp. 21-22 infra.)

It is undisputed that from 1974, when the use of the premises as a nursing home became nonconforming, until 1980, the premises were not used for any purpose. In the view of petitioners

Goldstein and Department of Buildings, this nonuse for a period of six (6) years constituted an abandonment of the nonconforming use by operation of law.*

In 1975, debtor had acquired title to the property. In June 1977, the mortgagee commenced foreclosure on its mortgage and entered a judgment of foreclosure. Just before the date scheduled for the sale, the debtor filed a petition for a real property arrangement under Chapter XII of the Bankruptcy Act, 11 USC §§801-926, obtaining an automatic stay of foreclosure by virtue of Bankruptcy Rule 12-43.

*Injunctive relief against the violation of a zoning ordinance may be obtained by a municipality against an illegal use, irrespective of the non-revocation of a C.O. 3 Rathkopf, The Law of Zoning and Planning, Sec. 55-22.

In March 1978, the trustee obtained the agreement of the State Department of Health that establishment approval for a nursing home may be granted to a religious group which can demonstrate a need for a nursing home for its adherents. The Trustee then entered into a contract to sell the facility to Beth Rifka, a Hassidic Jewish organization, conditioned upon Beth Rifka's ability to obtain all necessary licenses and certificates. Beth Rifka obtained such approval in September 1980, and commenced operations in March 1981, during the pendency of this litigation.

Prior to April 1980, community groups opposed to the nursing home called the attention of petitioner Goldstein to a possible violation of zoning regulations by use of the facility as a nursing home based upon the abandonment of the

facility by two years of non-use. Goldstein, after consultation with his superiors in the New York City Department of Buildings, agreed with this view and, in April 1980, commenced proceedings before the New York City Board of Standards and Appeals (BSA) to revoke the C.O. Under the New York City Charter, §645(b)(3)(e), a C.O. is presumptively valid until revoked by the BSA or by a court of competent jurisdiction. As will be discussed below, the BSA proceedings were interrupted by the injunction order issued by the bankruptcy judge.

In granting injunctive relief, Bankruptcy Judge Galgay* held that the petitioners violated the automatic stay by commencing revocation proceedings without leave of his court, but, treating the City's papers as a motion to vacate the automatic stay, denied such relief because the City had not shown any legitimate need to enforce its zoning regulations in the instant case. He gave great weight to the State's finding that there was a need for a nursing home for the Hassidic community. Although Judge Galgay did not make any specific findings of "bad faith", he did find that the City official's revocation efforts were belated and initiated in response to pressure by community groups. He concluded that

* A copy of his opinion is contained in Appendix C.

under §411 of the Bankruptcy Act, he could permanently enjoin revocation of the C.O. even after transfer of title to Betn Rifka.

The City appealed to the District Court. On appeal, Judge Leval reversed the order of Judge Galgay on the ground that enforcement of police powers such as zoning is outside the jurisdiction of the Bankruptcy Court, citing Sec. 362 of the 1978 Bankruptcy Code in support of his conclusion.* Furthermore, he noted the tendency of bankruptcy courts to put a higher premium on rehabilitation of debtors than on uniform enforcement of regulatory powers of the State which may endanger the success of the reorganization and doubted whether such courts were the appropriate neutral forum to decide these issues.

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* A copy of his opinion is contained in Appendix B.

The Trustee appealed to the Second Circuit and that court reversed Judge Leval and remanded the case to the District Court for review of the bankruptcy court's finding of bad faith on the part of petitioners. The Court of Appeals explained that by bad faith it meant more than an erroneous determination of law or fact but rather a showing by the Trustee that the City seeks to enforce a law which is "flagrantly and patently violative of express constitutional prohibitions"; that the state forum is biased; that the City acted in wilful disregard of the law; that City officials clearly abused their discretion in initiating proceedings against the trustee; that the City's motivation was a desire to harass, by ill will, or by any other improper motive (A27-28). The court noted that a proceeding commenced by City officials in the

usual manner upon notification of a violation would not evidence bad faith (A28, 29).

The Circuit Court held that Bankruptcy Rule 12-43, which bars commencement of a proceeding to enforce a lien against the debtor's property, was sufficiently broad to stay the City's attempted revocation of the Debtor's C.O., since the nursing home was its sole asset and critical to its reorganization (A19). It viewed §645 of the New York City Charter, wnich makes a C.O. binding upon City agencies (until revoked or modified by the Board of Standards and Appeals or a court), as investing a property-like quality to the C.O., despite its mere evidentiary nature (A19-20). It therefore concluded that the City officials had to petition the Bankruptcy Court to relieve the City from the stay and demonstrate cause for

such relief (A20). It distinguished its own decision in Smith v. New York State Liquor Authority, In Re Bay Ridge Inn, Inc. 94 F2d. 555 (2d Cir. 1935), in which it had held that a bankruptcy court had no power to compel the State Liquor Authority to reinstate a liquor license to a debtor on the ground that no bad faith was alleged there, whereas in the present case the Bankruptcy Court had made a finding that the City's conduct was not a legitimate exercise of police power (A23-24).

It went on to hold that §362 of the new Bankruptcy Code was not a codification of existing law under the Act, but rather a legislative expression of preference for a narrower application of the automatic stay in the future. It further held that even under §362 the Bankruptcy Court retained power to

enjoin bad faith enforcement of a local regulation, even if the automatic stay was inapplicable, and that Congress did not adopt a total hands-off approach towards local regulation (A24-25).

The dissent of Circuit Judge Mansfield pointed out that the Trustee did not even assert a claim of denial of the debtor's constitutional rights and that enforcement of State laws should be left to the State's administrative apparatus, with the debtor having the same right to judicial review as any other party (A32). A bankruptcy court should not be a super-Planning Commission or Board of Standards and Appeals (A32). The dissent pointed out that the State administrative agencies and courts were not only better equipped to determine the issues, but that there was a fundamental conflict between a

bankruptcy court's interest or motivation -- to rehabilitate the debtor for the benefit of creditors -- and that of a state agency whose interest is a fair and uniform enforcement of regulatory powers which benefit the community at large (A34). Judge Mansfield pointed out that, if bankruptcy courts interfered with State regulatory agencies wherever threatened action adversely affected the value of the debtor's estate, it would work havoc with many State laws (A34-35). He disputed the applicability of Bankruptcy Rule 12-43 to such cases, since the purpose of the rule was to prevent lien enforcement by secured parties from thwarting reorganization. He raised doubt as to whether a

C.O. could be classified as "property"* especially where the legality of the use lapsed by its non-exercise through the nonuse of the facility for over two years (A37-40). Finally, he found nothing in the record showing any bad faith on the part of the petitioners (A43-46).

* A C.O. is merely a piece of paper evidencing the existence of certain facts at the time it was issued.

APPLICABLE STATUTES AND RULES

Bankruptcy Act of 1898, as amended*

> §1. Creation of courts of bankruptcy and their jurisdiction
>
> (a) The courts of the United Stated hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this title, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to -
>
> * * *
>
> (15) Make such orders, issue such process, and enter such judgments, in addition to those specifically provided for, as may be necessary for the enforcement of the provisions of this title: Provided, however, That an injunction to restrain a court may be issued by the judge only;
>
> * * *

*All petitions filed prior to October 1, 1979 are governed by the Act, as is the instant action since the petition was filed in 1977. The Bankruptcy Code governs petitions filed on and after October 1, 1979. P.L. 95-598, Sec. 403(a).

(20) Exercise ancillary jurisdiction over persons or property within their respective territorial limits in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other court of bankruptcy: Provided, however, That the jurisdiction of the ancillary court over a bankrupt's property which it takes into its custody shall not extend beyond preserving such property and, where necessary, conducting the business of the bankrupt, and reducing the property to money, paying therefrom such liens as the court shall find valid and the expenses of ancillary administration, and transmitting the property or its proceeds to the court of primary jurisdiction; ....

§411. Exclusive jurisdiction of debtor and property

Where not inconsistent with the provisions of this chapter, the court in which the petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and his property, wherever located.

PERTINENT PROVISIONS OF THE NEW YORK CITY ZONING RESOLUTION

Section 12-10 of the Zoning Resolution contains the following definitions of "non-conforming" use and "non-conforming":

> A "non-conforming" use is any lawful use, whether of a building or other structure or of a tract of land, which does not conform to any one or more of the applicable use regulations of the district in which it is located, either on the effective date of this resolution or as a result of any subsequent amendment thereto.
>
> A non-conforming use shall result from failure to conform to the applicable district regulations on either permitted Use Groups or performance standards.
>
> A "non-conformity" is a failure by a non-conforming use to conform to any one of such applicable use regulations.

Sec. 52-61 of the Zoning Resolution provides:

> If, for a continuous period of two years, either the non-conforming use of land with minor improvements is discontinued, or the active operation of substantially all the non-conforming uses in any building or other structure is discontinued, such land

or building or other structure shall thereafter be used only for a conforming use. Intent to resume active operations shall not affect the foregoing.

The provisions of this Section shall not apply where such discontinuance is directly caused by war, strike or other labor difficulties, a governmental program of materials rationing, or the construction of a duly authorized improvement project by a body or a public utility company.

REASONS FOR GRANTING THE WRIT

(1)

Petitioners submit that a writ of certiorari should issue because the Second Circuit's decision of August 17, 1981 involves important unsettled issues of bankruptcy court jurisdiction and its relationship to enforcement by governmental bodies of their police and regulatory powers before administrative bodies and in non-bankruptcy courts. The subject has

been a source of conflicting decisions of the lower courts, on Bankruptcy, District and Circuit levels, and it is important that this conflict be expeditiously resolved to avoid confrontations between state and federal courts over these issues.

Petitioners note that there is presently pending before this Court a petition by the State of Missouri, et al. (No. 81-79, Oct. 1981 Term) for a writ of certiorari to the Eighth Circuit. We respectfully submit that the Missouri petition raises similar jurisdictional issues. If a writ is issued in that case, a writ should be issued in this case as well and oral argument on both cases could be scheduled for the same time. However, even if the petition of the State of Missouri is denied because this Court agrees with the holding of the

Eighth Circuit that Missouri's grain law does not properly fall into the classification of "police and regulatory laws", it should grant the petition herein because enforcement of zoning laws is clearly enforcement of the State's police powers. Indeed, the Eighth Circuit itself, at 647 F.2d 768, 778 (Appendix A-13 of Missouri's petition), cited District Judge Leval's decision in the instant case in its discussion of which types of governmental regulatory activities were excluded from the scope of the automatic stay. The Eighth Circuit stated (647 F.2d at 775):

> The present stay provisions [of the new Code] amplify and clarify provisions of the former bankruptcy law and bankruptcy rules provides for an automatic stay of certain proceedings against debtors. See, e.g. 11 U.S.C. 148 (repealed 1978); 11 U.S.C. §248 (repealed 1978); Rules of Bankruptcy Procedure 401, 601,

10-601, 11-44, 12-43 and 13-401. These automatic stays did not apply generally to proceedings affecting the public health and safety or certain governmental regulatory activity. See In Re Shippers Interstate Service, 618 F. 2d 9, (7th Cir. 1980) (labor laws); In re Bel Air Chateau Hospital 611 F.2d 1248 (9th Cir. 1979) (labor laws); In re National Hosptial and Institutional Builders Co. 9 B.R. 948 (S.D. N.Y. 1981) (zoning laws); In re Grand Spaulding Dodge Inc., 5 B.R. 581 (Bankruptcy Ct. N.D. Ill 1980) (consumer protection laws); In re Canarico Quarries, Inc. 466 F. Supp. 1333 (D. Puerto Rico 1979) (environmental protection laws); In re Colonial Tavern, Inc., 420 F. Supp. 44 (D. Mass. 1976) (liquor laws). [Underlining added.]

The Eighth Circuit quoted from the legislative history of §362 of the 1978 Code to explain the

purpose of excluding police and regulatory law enforcement from the automatic stay.*

In all of the cases cited by the Eighth Circuit, the automatic stay under the Act was held to be inapplicable to matters of police and regulatory enforcement. In addition to these cases, the Sixth Circuit recently held that bankruptcy courts had no jurisdiction to pass on the validity of workers' claims for injury or death as the exclusive jurisdiction is vested in State courts in cases involving police powers. State of Ohio v. Mansfield Tire and Rubber Co, ___F.2d___, Bankruptcy Law Reports, CCH, §68,356 (Sept. 29, 1981). In contrast, the Second Circuit decision in the instant case appears to be alone in holding that

*When Congress enacted the 1978 Code, it also enacted 28 U.S.C. §1478 as an explicit jurisdictional bar to removal to a Bankruptcy Court of civil actions brought by a governmental unit to enforce its police and regulatory powers.

the automatic stay applied to the enforcement of police power laws.

Apart from the conflict of the Second Circuit holding in the instant case with the numerous authorities cited by the Eighth Circuit (at p. 26, supra,) the holding is inconsistent with the judicial philosophy expressed by this Court in Palmer v. Massachusetts, 308 U.S. 79 (1939), in which the Court held that a bankruptcy court cannot usurp the functions of a state railroad commission and permit a railroad in reorganization to abandon local service. This Court noted that in construing legislation involving operation of railroads owned by a debtor, the Court traditionally upheld the power of States to regulate their local transportation and, in the absence of a clear Congressional mandate to the

contrary, reorganization courts could not interfere in such matters (id. at 83-84). This Court rejected arguments that continuance of state control over local passenger service would impair the power of the bankruptcy court to formulate a reorganization plan for I.C.C. approval, noting that a single judge removed from familiarity with local problems, and not necessarily gifted with statesman-like imagination, should not override decisions of expert state agencies [id. at 89].

If the Second Circuit opinion is not altered, the City could not issue a "vacate order" on a building it believes to be hazardous to life and limb without first obtaining leave of a Bankruptcy Court if such building happened to be owned by a debtor. If the Bankruptcy Court is located outside of the City (perhaps

thousands of miles away), the City must then expend considerable time and money just to seek leave from a distant bankruptcy judge before it can protect its citizens. This result undermines the City's ability to protect the very lives of its citizens in an emergency. Moreover, as District Judge Leval pointed out in his opinion (at B7-8), the fact that one has filed in bankruptcy should not exempt him from jurisdiction of local traffic courts or criminal courts if he drives the wrong way on a one-way street or commits a criminal assault.

As noted by Judge Leval, if bad faith can be shown by the trustee, he has adequate judicial remedies in the state courts or even in a federal court under civil rights statutes (B16 n. 7).

It should be further noted that Bankruptcy Judge Galgay held no hearings and all his findings of facts were based on papers submitted by the parties. All that the City conceded is that it took no action to revoke the C.O. until 1980, when some local community groups called the violation to its attention. Since the City is unable to police all zoning violations, it must necessarily depend on citizen complaints for much of its enforcement. The majority opinion concedes that response to citizen complaints is not an indication of bad faith (at A28-29). And, as the dissent points out, there was no actual existing violation of law because the debtor was not even using the property as a nursing home and might never have done so (at A44-46). Thus, there is nothing in the record to support the Trustee's allegations of bad faith.

Another issue on which the Second Circuit's ruling conflicts with that of another Circuit, the Third Circuit, is whether a C.O. is "property" of the debtor within the constructive custody of the court. In the present case, the majority treated a certificate as valuable property even though it was only evidentiary in nature (A19). In In Re Dolly Madison Industries Inc., 504 F.2d 499 (3rd Cir. 1974), the Third Circuit held that a certificate of authority to do business in a certain state was not property, citing Gills v. California, 293 U.S. 62 (1934), in which this Court held that a bankruptcy court was powerless to authorize non-compliance with a state licensing statute.

As shown at pp. 8-9, supra, the City's zoning law is self-executing and, upon nonuse of the facility as a nursing home for two years, the legality of its use lapsed ipso facto, irrespective of the outstanding C.O. This lapse occurred in 1976, more than a year before the petition was filed. The City was thus entitled to obtain injunctive relief against use of the property as a nursing home. 3 Rathkopf The Law of Zoning and Planning §55-22. The C.O. itself cannot properly be characterized as "property" within the constructive custody of the court.

Moreover, Bankruptcy Judge Galgay's injunction appears to extend beyond the duration of the debtor's ownership of the facility, and to affects the property permanently even after it is transferred to other parties. The effect

of such an injunction order would be to permanently prevent the City from enforcing a violation of zoning laws long after the debtor is gone from the scene. The result of such an order is absurd.

Even during debtor's ownership, a Trustee, as are all court officers, is obligated to manage and operate property in his possession in accordance with the valid laws of the state in which the property is situated in the same manner as any other property owner. 28 U.S.C. §959(b). The courts have no power to dispense with this statute.

CONCLUSION

For these reasons, a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

Opinion of the Court of Appeals

UNITED STATES COURT OF APPEALS
For The Second Circuit

*

No. 1301 --September Term, 1980
(Argued April 29, 1981 Decided
August 17, 1981)
Docket No. 81-5009

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In The Matter of
NATIONAL HOSPITAL AND INSTITUTIONAL BUILDERS COMPANY, a Partnership,
Debtor.

NATIONAL HOSPITAL &
INSTITUTIONAL BUILDERS Co.,
Plaintiff,

JAMES L. GARRITY, Trustee of the Debtor,
Appellant,

--v.--

PHILIP GOLDSTEIN, NEW YORK CITY DEPT. OF BUILDINGS, and NEW YORK CITY BOARD OF STANDARDS & APPEALS,

Defendants-Appellees.

*

B e f o r e:

LUMBARD, MANSFIELD, and VAN GRAAFEILAND,

Circuit Judges.

The Debtor's trustee in bankruptcy appeals from an order of the Southern District, Leval, J., which reversed an order of Bankruptcy Judge Galgay who had enjoined the City of New York under the automatic stay provision of Bankruptcy Rule 12-43 from seeking revocation of the Debtor's Certificate of Occupancy.

Reversed and remanded for further findings of facts.

ARTHUR S. OLICK, ESQ., New York, N.Y. (Anderson Russel Kill & Olick, P.C., James P. Heffernan, Esq., Tina L. Wellner, Esq., New York, N.Y., of counsel), for Appellant.

JUDAH DICK, Assistant Corportion Counsel,

New York, N.Y. (Allen G. Schwartz, Corporation Counsel, Leonard Koerner, Joseph I. Lauer, Marvin B. Mitzner, New York, N.Y., of counsel), for Appellees.

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LUMBARD, Circuit Judge:

James L. Garrity, acting as trustee for the National Hospital and Institutional Builders Company (Debtor), appeals from an order of Judge Leval of the Southern District reversing an order of the bankruptcy court. Bankruptcy Judge Galgay had applied the automatic stay imposed by Rule 12-43 of the Rules of Bankruptcy Procedure to prohibit the appellees -- various subdivisions and officers of the City of New York -- from instituting or continuing proceedings to revoke the Certificate of Occupancy for the Debtor's nursing home. Because the district court failed to review Bankruptcy Judge Galgay's critical finding that the City was pursuing the revocation in bad faith, we reverse and remand for further findings of fact.

The Debtor, a New York partnership, owns as its sole asset a nursing home and the land it occupies at 1000 Targee Street on Staten Island. The Debtor's four partners were Bernard Bergman and three members of his family. The New York City Department of Health initially granted approval for establishing the nursing home in April of 1966, and construction began in June of 1969. Construction was completed in June of 1973, and a final Certificate of Occupancy (C.O.) was issued in June of that year. Washington Heights Federal Savings and Loan Association (Washington Federal) held a mortgage on the property of approximately $2 million.

In 1975, Bergman was indicted by a federal grand jury for filing false tax returns, submitting false medicaid claims, making false statements to the federal government, and conspiring to commit those offenses and to defraud the government. He was also indicted by a New York State grand jury for conspiracy, filing fraudulent reimbursement claims, larceny, and obstruction of government administration. Bergman pled guilty to a violation of the New York Public Officers Law as part of a larger plea agreement that settled both the federal and state indictments against him. Under that agreement, Bergman's assets, which included his interest in this and several other nursing homes, were assigned to a state-appointed

receiver for purposes of collecting a $2.5 million judgment against Bergman held by the State. See Chase Manhattan Mortgage and Realty Trust v. Bergman (In re Bergman), 585 F.2d 1171 (2d Cir. 1978).

From the building's completion until late 1979, the State of New York, which regulates the establishment and construction of nursing homes, had denied the approval necessary for the nursing home to open. The State contended that the initial establishment of the nursing home in 1966 was improper and that there was an excess of nursing home beds in Richmond County. Because the State denied that approval, the nursing home remained unopened, and the Debtor defaulted in its mortgage and tax payments.

On June 8, 1976, Washington Federal, the Debtor's mortgagee and principal creditor, commenced an action to foreclose in the Supreme Court of the State of New York, County of Richmond. On May 20, 1977, Washington Federal entered into an agreement with the City of New York to pay the delinquent real estate taxes and other assessments levied against the property. A final judgment of foreclosure and sale was entered on July 1, 1977, and the foreclosure sale was scheduled for September 1, 1977. On August 31, 1977, the Debtor filed its petition for an arrangement under Chapter XII of the Bankruptcy Act, 11 U.S.C. §§801-926, and the Bankruptcy Court notified all creditors, including the City of New York, of the filing of the petition. The automatic stay provision of Bankruptcy Rule 12-43 prevented the foreclosure sale scheduled for the next day.

On October 17, 1977, James L. Garrity was appointed trustee upon the Debtor's application. Faced with the State's continued refusal to approve the nursing home's establishment, Bankruptcy Judge Galgay directed Garrity to investigate other possible uses of the facility. In March of 1978, Garrity discussed with the New York State Department of Health the possibility of selling the nursing home to an Hassidic Jewish organization, and the Department agreed that it would be willing to authorize such a group to establish the home under the religious group exception to the State's public-need requirement.

On July 18, 1978, Garrity executed a contract with Beth Rifka, Inc., the Hassidic group, for the sale of the nursing home. The parties established as a condition precedent,

however, the granting of establishment approval and various other state and federal approvals. On August 24, 1979, after both Beth Rifka and Garrity had submitted information to and answered questions from various health-care bodies, the Public Health Council of the State of New York, the final state licensing authority, granting Beth Rifka's application for establishment approval subject to several minor conditions. Because of certain improper procedures on its own part, the Public Health Council afterwards rescinded its approval, resubmitted the application, and approved it once again on December 21, 1979.

During the next several months, the parties arranged financing for the sale and eventually came to an accord. However, because

interest rates had risen substantially between the Health Council's approval and the spring of 1980, Beth Rifka had to obtain an additional approval from the Health Council. This final approval was obtained on September 19, 1980, and the sale was ready to be consummated, thus providing the economic foundation for the Bankruptcy Court's Chapter XII plan of arrangement.

However, a few months before the State granted the final approval and seven years after the final C.O. was issued by the City, the New York City Department of Buildings first suggested that it might initiate proceedings to invalidate the nursing home's C.O. Borough Superintendent of Buildings Philip Goldstein raised this possibility in a letter of May 7, 1980 which stated that the Debtor's intended

use of the facility was a non-conforming use and that therefore he would initiate proceedings before the Board of Standards and Appeals to revoke the C.O. Under Goldstein's view of the City zoning law, the nursing home became a nonconforming use when the zoning ordinances were amended in 1974, after the C.O. was granted; and nonconforming uses forfeited their C.O.'s if they did not do business for two years, as the Debtor's nursing home clearly had not.

On June 11, 1980, Garrity's counsel advised Goldstein that the Department of Buildings was stayed, pursuant to Bankruptcy Rule 12-43, from appealing to the Board of Standards and Appeals to revoke the C.O. Goldstein thereafter advised Garrity's counsel that he intended to proceed with the revocation

on the advice of the Department's counsel that the automatic stay was inapplicable. In a letter dated August 4, 1980, Goldstein applied to the Board of Standards and Appeals for such revocation without leave of the bankruptcy court. He also stated, however, that Garrity could reobtain a C.O., despite that nonconforming use, merely by requesting a Special Permit from the Board. He added that the City did not intend to oppose the grant of the Special Permit. Thus, Goldstein's letter requested revocation of the C.O. but established that the City's interest was not sufficient for it to oppose a Special Permit that would nullify the revocation.

By an order to show cause dated August 7, 1980, Garrity moved in the bankruptcy court for an order staying Goldstein, the

Department of Buildings, and the Board of Standards and Appeals from instituting or continuing proceedings to revoke the Debtor's C.O., or, in the alternative, for an order adjudging Goldstein in contempt of the automatic stay imposed by Rule 12-43. Because the parties did not dispute the material facts, the bankruptcy court did not take testimony but rather invited the parties to submit proposed findings. By order dated October 8, 1980, Bankruptcy Judge Galgay granted Garrity's motion

for injunctive relief and denied the alternative order of contempt. He first held that the C.O. was "property" within the exclusive jurisdiction of the bankruptcy court under section 411 of the Bankruptcy Act. He then held that Bankruptcy Rule 12-43's automatic stay of state proceedings against a debtor's property therefore applied to this Debtor's C.O. Finally, he held that the City had failed to demonstrate the good cause required for the court to vacate the stay and that the facts demonstrated that the proposed revocation of the C.O. was not a valid exercise of the police power. The bankruptcy court based that finding of bad faith on two observations. First, Bankruptcy Judge Galgay found that the City's attempted revocation was not undertaken to protect the public health and welfare of the surrounding community because, if that had been

the true concern, it would not have taken seven years for the City to act. Indeed, Goldstein began the proceedings only after being prodded by three community organizations which Garrity asserts were motivated by a dislike of Hassidic Jews. Second, Bankruptcy Judge Galgay noted that the State of New York had extensively reviewed the needs of the region and of the Hassidic population, and it had concluded that the Debtor's facility would fulfill an unmet need in the community. He then held that the State's interest in administering health care was greater than the City's interest in having the Debtor obtain a Special Permit (which the City did not intend to oppose) to replace the C.O.

On February 16, 1981, while the appeal to the district court was pending, Garrity opened the nursing home, and it admitted patients for the first time.

Judge Leval reversed the order of the bankruptcy court. He concluded that state regulatory power was beyond the scope of the bankruptcy court's exclusive jurisdiction. Accordingly, the bankruptcy court could not interpret Rule 12-43's automatic stay in a manner that precluded the revocation. The district court made no finding of fact regarding the good faith of the City's conduct. Because we believe the City's good faith to be critical to this case, we reverse and remand to the district court for findings of fact on that issue.

Bankruptcy Rule 12-43, which was in effect at the time the Debtor filed its Chapter XII petition, provides that the petition "shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor...or of any court proceedings to enforce any lien against his property." We find Rule 12-43 sufficiently broad to stay the City's intended revocation of the Debtor's C.O. The nursing home is the Debtor's sole asset, and its establishment is critical to the Debtor's economic recovery. The C.O. which the City seeks to revoke represents the City's commitment that, when the C.O. was issued, the nursing home could legally be used for its intended purpose: 645(e) of the New York City Charter provides that a C.O. is "binding and conclusive upon

all agencies and officers of the city . . . unless and until the certificate is set aside, vacated or modified by the board of standards and appeals or a court of competent jurisdiction." Given the importance of the C.O. to the Debtor and the substantial weight the C.O. is accorded by the City, we cannot say that Goldstein's application for revocation is any less a "proceeding against the debtor" than a court proceeding or a pending arbitration. See Rule 12-43 of Bankruptcy Procedure, Advisory Committee Notes. Accordingly, the City's attempted revocation of the C.O. was stayed by the filing of the Debtor's petition in bankruptcy.

To proceed with the revocation, the City must petition the bankruptcy court and demonstrate cause for relieving it from the

automatic stay under Bankruptcy Rule 12-43(d), (e). Proof of good cause would obviously include proof that the revocation was being sought in good faith under state and federal law. This court's opinion in Smith v. New York State Liquor Authority (In re Bay Ridge Inn, Inc.), 94 F.2d 555 (2d Cir. 1938) does not suggest that bankruptcy courts must defer to bad faith local regulation. In Bay Ridge Inn, the New York Liquor Authority had issued the debtor a liquor license scheduled to expire one year from its issuance on October 1, 1936, and the debtor filed its petition in bankruptcy in January of 1937. The Liquor Authority revoked the debtor's license and denied it any refund upon its license in June of 1937. The Debtor apparently did not dispute in the district court that (1) it had never paid the deposit that was

required to be paid within 30 days of the license's issuance; (2) it had attempted to assign the license in February of 1937 although the Alcoholic Beverage Control Law compelled revocation as a penalty for any attempt to assign; and (3) the custodian of the debtor's inn had been arrested for selling liquor during prohibited hours. On March 1, 1937, the debtor's trustee surrendered the license to the Liquor Authority to obtain a refund of $685.00. On June 1 of that year, however, the Authority concluded that the debtor had violated the Beverage Control Law in three instances, revoked the debtor's license, and denied it any refund because refunds were not available when a license was cancelled for violation of the Beverage Control Law. The debtor, attempting to salvage its refund, obtained an order from the

district court in September of 1937 which annulled the Authority's decision.

This court reversed the district court order. There was no evidence that the Authority had acted in bad faith, and this court held that the debtor's remaining rights to a refund were properly to be determined by state tribunals.[1] Unlike Bay Ridge Inn, the debtor here is supported by the factual finding of the bankruptcy court that the City's conduct was not a valid exercise of its police power. Thus, this case presents an entirely different issue than was presented in Bay Ridge Inn, and the

[1] Colonial Tavern, Inc. v. Byrne (In re Colonial Tavern, Inc.), 420 F. Supp. 44 (D. Mass. 1976) also did not involve any assertion of bad faith on the part of state and local officials. Similarly, doctrines of federal abstention in deference to state proceedings have consistently not applied in cases of bad faith conduct by the state. See Juidice v. Vail, 430 U.S. 327, 338 (1977); Huffman v. Pursue, Ltd., 420 U.S. 592, 611 (1975); Younger v. Harris, 401 U.S. 37, 53-54 (1971).

district court must review the finding of bad faith before determining whether the Debtor's only resort here lies in state and local proceedings.

The City argues that the new Bankruptcy Code dictates a different outcome in this case because it specifies that the automatic stay does not apply to proceedings by governmental units to enforce their police or regulatory powers. See 11 U.S.C. §362. We disagree. First, as the City concedes, the earlier Bankrupcty Act, not the new Code, controls in this case because the petition was filed under the Act. See Guardian Mortgage Investors v. Unofficial Noteholders-Debenture-holders Creditors Committee, 607 F.2d 1020, 1023 n.6 (2d Cir. 1979). Second, Congress's determination that the new Code's stay provision

should not preclude enforcement of local regulation provides little direction for interpreting the stay under the Act. Instead of revealing its earlier intentions under the Act, Congress may simply have been expressing its preference for a narrower, rather than broader, application of the automatic stay in the future. Compare Katman v. New Jersey, 13 C.B.C. 524 (D.N.J. 1977); In re Hillsdale Foundry Co., 2 C.B.C. 542 (W.D. Mich. 1974), with Colonial Tavern, Inc. v. Byrne, 420 F. Supp. 44 (D. Mass. 1976). Third, Congress removed local regulation only from the effect of the automatic stay; it did not eliminate the bankruptcy court's power to enjoin the enforcement of local regulation which is shown to be used in bad faith. Thus, although it addressed the issue, Congress did

not adopt the total hands-off approach toward local regulation that the City advocates here.

Finally, we do not believe that Congress, under either the Act or the Code, intended to prohibit bankruptcy courts from protecting a debtor's assets from bad faith zoning regulation. If courts lacked that power, a city interested in the outcome of a bankruptcy petition could seriously interfere with management of the bankrupt estate through repeated threats of harmful rezoning. The Constitution authorizes Congress to establish uniform laws of bankruptcy, U.S. Const., Art. I, §8, and it establishes that laws passed pursuant to the Constitution are the supreme law of the land, U.S. Const. Art. VI. Those grants of authority surely include the power to thwart bad faith frustration of federal bankruptcy policy.

On remand, upon the City's motion for relief from the automatic stay, the district court should review the bankruptcy court's finding of bad faith on the part of the City. We note that bad faith here means more than an erroneous determination of law or fact. Rather, the trustee must show, for example, that the City seeks to enforce a law that is "'flagrantly and patently violative of express constitutional prohibitions in every clause, sentence or paragraph, and in whatever manner and against whomever an effort might be made to apply it,'" Younger v. Harris, 401 U.S. 37, 53-54 (1971); that the state forum is biased, e.g., Gibson v. Berryhill, 411 U.S. 564, 93 S.Ct. 1689, 36 L.Ed. 2d 488 (1973); see McCune v. Frank, 521 F.2d 1152, 1158 (2d Cir. 1975); that the City acted in wilful disregard of the

law; that City officials clearly abused their discretion in initiating proceedings against the trustee; or that the "state proceeding [was] motivated by a desire to harass," Huffman v. Pursue, Ltd., 420 U.S. 592, 611 (1975), by ill will, or by any other improper motivation, cf. Central Avenue News, Inc. v. City of Minot, No. 80-1521, slip op. at ____ (8th Cir. Feb. 10, 1981) and Eagle Books, Inc. v. Reinhard, 418 F. Supp. 345, 351 (N.D. Ill. 1976), vacated on other grounds, 432 U.S. 902 (1977) ("The gravamen of bad faith prosecution is the lack of a reasonable expectation that valid convictions will result"). Of course, if the City shows that its officials proceeded in the usual manner upon notification of events requiring official response, there would be no evidence that the

City acted in bad faith.[2]

Contrary to the City's assertions, it is neither unseemly nor unusual for the bankruptcy court to examine issues of state zoning law to determine whether the intended revocation is marred by procedural or substantive defects. We emphasize that the purpose of the bankruptcy laws -- to allow the

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[2] If a private citizen instigated the proceeding against the debtor to harass or coerce the debtor in an unrelated matter, the trustee may have a cause of action for damages against that party for malicious abuse of legal process. See 1 F. Harper & F. James, The Law of Torts §4.9, at 330-31 (1956).

trustee without delay to marshal and administer the assets of the debtor -- would be frustrated were state officials free to interfere with the administration of the bankrupt's estate through bad faith zoning regulation. Nor is it reasonable to require the bankruptcy court to await the correction of such abuses by the state courts. The attendant delay itself might permanently damage the estate through the inevitable dissipation of skilled personnel and goodwill. Hence, if the City's intended revocation is in bad faith, the bankruptcy court's injunction should stand.

Accordingly, we reverse and remand for proceedings consistent with this opinion.

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MANSFIELD, Circuit Judge (Dissenting):

I respectfully dissent for reasons that are well stated by Judge Leval in his opinion and order dated February 25, 1981, dissolving the injunction issued by the Bankruptcy Court, Galgay, J., barring New York City officials from seeking to revoke a certificate of occupancy that had permitted the establishment of a nursing home on the debtor's property. In my view the Bankruptcy Court lacks jurisdiction to interfere with the state's enforcement of its regulatory powers. See Smith v. New York State Liquor Authority, Inc. (In re Bay Ridge Inn, Inc.), 94 F.2d 555 (2d Cir. 1938); NLRB v. Jonas (In re Bel Air Chateau Hospital, Inc.), 611 F.2d 1248 (9th Cir. 1979); Colonial Tavern, Inc. v. Byrne (In re Colonial Tavern, Inc.), 420 F. Supp. 44 (D. Mass. 1976).

Absent some claim of denial of the debtor's constitutional rights -- and none is asserted here -- those state police powers resi within the exclusive jurisdiction of the state's administrative apparatus, with the debtor having the same right as any other citizen to obtain state judicial review. A federal bankruptcy court is not a super-City Planning Commission or Board of Standards and Appeals.

Nothing in the Bankruptcy Act confers upon the Bankruptcy Court, a statutory tribunal of limited jurisdiction, any of the powers which the majority would permit it to exercise here. Strong federal-state comity considerations militate against federal intervention into state zoning matters that are not attacked on consitutional grounds. No showing is made that state remedies are inadequate. With due respect

for the able bankruptcy judge's expertise in bankruptcy matters, he would not ordinarily possess the qualifications of the appropriate state bodies to determine whether the City's zoning regulations would be violated, whether the nursing home here would "fulfill an unmet need in the community," and whether any benefit a nursing home would confer is outweighed by other considerations, such as excessive burdens on the community, traffic congestion, lack of adequate parking space or roads, inadequate off-street loading facilities, or the like. These are matters that the appropriate City administrative facility and state court are in a much better position to evaluate than a bankruptcy judge.

Aside from its lack of expertise and qualifications to determine the reach of local

zoning regulations, the Bankruptcy Court should not for another reason be empowered to enjoin the state's exercise of its regulatory powers. There is a fundamental conflict between a bankruptcy court's interest or motivation and that of the appropriate state tribunals. The Bankruptcy Court, naturally enough, is solely interested in enhancing the value of the debtor's estate for the benefit of creditors whereas the objective of state zoning bodies is to enforce regulatory powers (whether they relate to clean air, traffic, housing, size of residence units, or type of land use) for the benefit of the community at large. Lastly, we should note that if the Bankruptcy Court can prevent a state regulatory agency from taking action that might lessen the value of the estate, nothing would prevent it from enjoining

the state from invoking other state laws that might affect the bankruptcy, such as those calling for revocation of a license for cause or lapse, prohibiting the erection of advertising signs, prescribing fire control or safety regulations, authorizing criminal proceedings, or the like.

The majority, as a jurisdictional basis for the Bankruptcy Court's action here, relies on the automatic stay provisions of Bankruptcy Rule 12-43. However, as Congress made clear in its later more detailed codification of the law in the new Bankruptcy Code, Rule 12-43 was never intended to permit a Bankruptcy Court to interfere with a governmental unit's enforcement of its police or regulatory power, see Bankruptcy Code §362(b)(4), 11 U.S.C. §362(b)(4). Moreover, as

Learned Hand has wisely warned, "it is a commonplace that a literal interpretation of the words of a statute is not always a safe guide to its meaning," Peter Pan Fabrics, Inc. v. Martin Weiner Corp., 274 F.2d 487, 489 (2d Cir. 1960). Equally appropriate for present purposes are his remarks in Guiseppi v. Walling, 144 F.2d 608, 624 (2d Cir. 1944)(concurring opinion), where he stated:

> "It does not therefore seem to me an undue liberty to give the section as a whole the meaning it must have had, in spite of the clause with which it begins . . . There is no surer way to misread any document than to read it literally; in every interpretation we must pass between Scylla and Charybdis; and I certainly do not wish to add to the barrels of ink that have been spent in logging the route. As nearly as we can, we must put ourselves in the place of those who uttered the words, and try to divine how they would have dealt with the unforeseen situation; and, although their words are by far the

> most decisive evidence of what they would have done, they are by no means final."

See also Federal Deposit Insurance Corp. v. Tremaine, 133 F.2d 827, 830 (2d Cir. 1943) (L. Hand, C.J.) ("There is no surer guide in the interpretation of a statute than its purpose when that is sufficiently disclosed; nor any surer mark of our solicitude for the letter than to wince at carrying out that purpose because the words used do not formally quite match with it"). The purpose of Rule 12-43 was to supplement and reinforce the Bankruptcy Court's exclusive jurisdiction over property in its possession in order to avoid creation or enforcement of liens by third parties.

It is questionable whether a Certificate of Occupancy may be classified as "property,"[1] but even if it were, it automatically ceased to exist as

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[1] Even if a Certificate of Occupancy is treated as a property right, it is expressly conditioned upon the power of the Board of Standards to vacate or modify it. Section 645(e) of the New York City Charter provides:

> "every certificate of occupancy shall, unless and until set aside, vacated or modified by the board of standards and appeals or a court of competent jurisdiction, be and remain binding and conclusive upon all agencies and officers of the city, and shall be binding and conclusive upon the department of labor of the state of New York, as to all matters therein set forth, and no order, direction or requirement affecting or a variance with any matter set forth in any certificate of occupancy shall be made or issued by any agency or officer of the city, or by the department of labor of the state of New York, or any commission, board, officer or member thereof, unless and until the certificate is set aside, vacated or modified by the board of

(footnote continue on next page)

a matter of law in the present case when it lapsed under New York City Zoning Resolution, §52-61,[2] by reason of the permittee's admitted non-exercise of

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standards and appeals or a court of competent jurisdiction upon the application of the agency, department, commission, officer or member thereof seeking to make or issue such order, direction or requirement...." (Emphasis supplied).

2 New York City Zoning Resolution, §52-61, provides in pertinent part:

> "If, for a continuous period of two years, either the non-conforming use of land with minor improvements is discontinued, or the active operation of substantially all the non-conforming uses in any building or other structure is discontinued, such land or building or other structure shall thereafter be used only for a conforming use. Intent to resume active operations shall not affect the foregoing."

the certificate for a continuous period of two years prior to 1976.

The majority, apparently recognizing that the automatic stay provisions of the Act may have no application, nevertheless asserts that the Bankruptcy Court has power to enjoin the "bad faith" enforcement of local state regulations.[3] I disagree. Such an exception would result in

[3] Appellant concedes that the Bankruptcy Court lacks jurisdiction to prevent good faith enforcement of state zoning regulations and contends that the issue is whether it has jurisdiction to enjoin bad faith enforcement, stating:

> "This Court is not, as the City suggests, faced with deciding whether a bankruptcy court is vested with power to prevent good faith enforcement of zoning regulations in order to protect health, safety and welfare. It is beyond peradventure that the bankruptcy court cannot and should not do so. Here the issue is the City's lack of good faith." (Appellant's Reply Br. at 1; emphasis in original)

Bankruptcy Court mini-trials of purely state regulatory issues whenever, as might be expected to happen frequently, the debtor sought by claiming "bad faith" to have those issues tried in a Bankruptcy Court, which would be sympathetic toward any resolution that would improve the estate, rather than before state tribunals. The proper remedy is to seek redress in the state courts, which may be expected not to tolerate bad faith conduct on the part of any regulatory officials.

Nor does the record in the present case support a claim that the Borough Superintendent of Buildings acted in bad faith. Although a Certificate of Occupancy was issued to the debtor on June 11, 1973, the property remained vacant for many years and was not operated as a nursing home until 1980. In the meantime, on January 10, 1974,

the City's Board of Estimate amended Zoning Resolution §74-90 to prohibit the use of property as nursing homes except by special permit granted by the City Planning Commission upon it making certain findings as to landscaping, topography, supporting neighborhood services, traffic and benefits to the community. Since the debtor's property had not, prior to January 10, 1974, ever been used as a nursing home, this use could not thereafter be permitted as a matter of right and must be treated as a "non-conforming" use, Zoning Res. §12-10, for which a special permit would be required under Zoning Res. §74-90. Moreover, under Zoning Res. §52-61 the right to use the property for a nursing home evidenced by the Certificate of Occupancy automatically lapsed and ceased to exist by reason of the non-use of the property as a nursing home for a continuous period of two years

after the issuance of the Certificate. All of these regulations are laws of general application which were not directed toward the debtor. The proposed revocation of the debtor's Certificate of Occupancy therefore amounts merely to a ministerial act mandated by the law. When his attention was brought to the existence of this non-conforming use, the Borough Superintendent of Buildings instituted the revocation proceeding now pending before the Board of Standards and Appeals.

In view of this undisputed history I find nothing in the record to suggest bad faith on the part of the Borough Superintendent of Buildings. Nor did Judge Galgay find bad faith, as the majority states; he found that the action was "not within the valid exercise of its police power under the zoning laws" because of the Borough Superintendent's delay in bringing the revocation

proceeding. To this appellant suggests bad faith based on the fact that the Superintendent was instigated to act by community complaints. In my view, to suggest that this indicates "bad faith" borders on the absurd. The delay in the City Department's institution of a ministerial action, when there was no existing violation of law because the debtor was not using the property as a nursing home and might never do so (in view of the continued refusal of the Public Health Council of the State of New York to grant a nursing home license), is so insignificant that it provides no basis for an inference as to later motive or intent. The Department of Buildings cannot be expected to be aware of all instances where such action is required. The fact that the lapse of the Certificate of Occupancy was brought to the Borough Superintendent's attention by a community group

opposed to the nursing home use and hence having an axe to grind does not taint the Borough Superintendent's motive or action. This is probably the most common manner in which threatened violations of law are brought to the attention of most law enforcement authorities, state or federal.

Finally, the best evidence that the Borough Superintendent, once the matter was brought to his attention, was merely doing his job, without fear or favor, lies in his advice to appellant Trustee that if the latter pursued the proper legal course by seeking a special permit for nursing home use from the City Planning Commission the Department of Buildings would not oppose the application. Indeed, since the City was under no obligation to remain neutral in the matter, this was evidence of the Borough Superintendent's good faith in enforcing the law. There is not one whit of evidence that in bringing the revocation proceed-

ing he was discriminating against appellant by permitting other similarly-situated holders of lapsed Certificates of Occupancy nevertheless to operate without such certificates.

For the foregoing reasons I would affirm the judgment of the district court.

APPENDIX B

Opinion of the District Court

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
- - - - - - - - - - - - - - - - X

In the Matter of

NATIONAL HOSPITAL AND INSTITUTIONAL BUILDERS COMPANY, a Partnership,

Debtor.

80 Civ. 6073

OPINION AND ORDER

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PIERRE N. LEVAL, U.S.D.J.

This is an appeal from a ruling of The Honorable John J. Galgay, Bankruptcy Judge,[1] holding that administrative efforts by The City of New York to revoke the Certificate of Occupancy of a nursing home owned by the debtor violated the automatic stay provisions of Rule 12-43 of the Rules of Bankruptcy Procedure, and enjoining the revocation proceedings under authority of Section 411 of the 1898 Bankruptcy Act, 11 U.S.C. § 811.

The basic facts are not in dispute. The debtor's sole asset is real property at 1000 Targee Street on Staten Island on which stands an unoccupied structure built as a nursing home for the aged. The New York City Department of Health gave its approval for the establishment of the nursing home in April, 1966. Construction of the home was begun by a prior owner in June, 1969. Construction was completed in 1973. In January and March 1973 temporary C.O.s were issued. In June 1973 a final C.O. was issued. However, the New York State Public Health Council of the New York State Department of Health declined to give the home "establishment approval" because of an excess of nursing homes on Staten Island.

The debtor acquired the property in 1975. In June 1977 the mortgagee of the building began a suit in New York State Supreme Court to

foreclose its mortgage. Judgment of foreclosure was entered, and the foreclosure sale was set for September 1, 1977.

One day before the foreclosure sale, the debtor filed a petition for a real property arrangement under Chapter 12 of the Bankruptcy Act, 11 U.S.C. §§ 801-926. The foreclosure sale was stayed by the automatic provision of Bankruptcy Rule 12-43.

In March 1978 the Trustee obtained the agreement of the New York State Department of Health that establishment approval might be granted under a special provision of New York law applicable to religious groups, N.Y., Pub. Health Law § 2801-a(3) (McKinney), if an Hassidic group could demonstrate a need for nursing homes among its adherents. The trustee then entered into a contract for the sale of the nursing home to Beth

Rifka, Inc., an Hassidic Jewish organization, conditioned upon Beth Rifka obtaining required licenses and certificates.

Beth Rifka applied to the State Department of Health for establishment approval, which was granted in September 1980.

In the meantime Staten Island community groups brought pressure on New York City governmental bodies, seeking to prevent the establishment of the nursing home. These efforts apparently were quite successful. In May 1980, Philip Goldstein, Borough Superintendent of the Department of Buildings, indicated his intention to institute proceedings before the Board of Standards and Appeals to revoke the Certificate of Occupancy. On August 4 he formally applied to the Board for revocation of the C.O.[2]

The trustee then moved in the Bankruptcy Court by order to show cause for a stay barring

Goldstein and the Board from revoking, or pursuing the proceedings to revoke, the C.O. As noted above, Judge Galgay, in a decision filed October 8, ordered the revocation proceedings stayed, from which decision this appeal is taken.[3]

Judge Galgay, after reviewing the history of the nursing home, made findings that the City's revocation efforts were belated and were in response to pressure by community groups, that the City did not believe in good faith that the home would endanger or harm the community or neighborhood, and that the State had an interest in having the home opened.

He concluded that the revocation proceedings were not valid exercises of the City's "police powers" under its zoning laws, and that the revocation efforts were, therefore, not exempt from the automatic stay of Rule 12-43.

Judge Galgay concluded it was an appropriate exercise of the Bankruptcy Court's powers to enjoin the revocation proceedings under §411 of the Bankruptcy Act which gives the Bankruptcy Court exclusive jurisdiction of the debtor and his property.

In my view, Judge Galgay's opinion failed to give proper deference to the rule that state regulatory power is beyond the scope of Section 411's exclusive grant of jurisdiction.

This statute, operating together with the mandatory stay provisions set forth in the rules of the various bankruptcy chapters, protects the debtor against multiple, uncoordinated suits brought in various jurisdictions by a multitude of claimants. It gives the debtor a certain breathing spell and permits him to meet the various claimants in a single forum in coordinated proceedings under the supervision of a single judge. The statute and

rule are motivated in part by the recognition that most estates would be torn apart by legal fees and chaos (to the disadvantage of all) if the debtor were required to answer every separate action in a separate proceeding in whatever court it may be asserted. See Fidelity Mortgage Investors v. Camelia Builders, Inc., (In re Fidelity Mortgage Investors), 550 F.2d 47, 55 (2 Cir. 1976), cert. denied, 429 U.S. 1093, reh. den., 430 U.S. 976 (1977).

Courts have long recognized, however, that a state's enforcement of its regulatory powers (sometimes called police powers) against the debtor or its property is a different kind of matter affected by different considerations. The fact that one has filed in bankruptcy should not exempt him from jurisdiction of the local traffic courts or criminal courts if he drives the wrong way on a one-way street or commits a criminal assault.

Similarly if a state administrative agency is charged with the responsiblity of establishing and enforcing an anti-pollution plan, it would not make sense to deprive the agency of power to enforce the plan against bankruptcy subjects, except at the sufferance of the Bankruptcy Court.

A state's (or municipality's) enforcement of its regulatory laws generally calls for uniform application consistent with an overall plan to achieve a desired effect, whether it be the achievement of clean air standards, preservation of the cleaniness of the town's drinking water, zoning for industry, commerce and residence[4] or whatever. The enforcement of these plans is ordinarily entrusted either to police, town council or specialized administrative body, with protection against unjust, discriminatory or illegal enforcement being entrusted to the local and state courts.

The concerns of such regulatory plans have generally little or nothing to do with the question of payment of debtors or with whether any subject is solvent or insolvent. Many such regulatory plans would be impaired, or at least applied in a chaotic irrational fashion, if the responsible administrative bodies were deprived of authority over any subjects which happened to be engaged in federal insolvency proceedings.

The responsibility and expertise of the Bankruptcy Court, in contrast, is to achieve orderly reorganization or distribution to creditors of the estates of bankrupts. It has nothing to do with the enforcement of state regulatory power. Nor is the ability of the bankruptcy court to supervise orderly liquidation or reorganization overcome if the bankrupt remains subject to local regulatory power.

For such reasons, it has been established for many years in court decisions that the jurisdiction of the Bankruptcy Court does not extend to the enforcement of state regulatory power.[5] The sign-post decision on this principle is the opinion of Judge A. N. Hand in 1938, in Smith v. New York State Liquor Authority, Inc., (In re Bay Ridge Inn, Inc.), 94 F.2d 555 (2 Cir.) reversing an attempt by the District Court in bankruptcy to overturn a forfeiture imposed on the bankrupt by the State Liquor Authority.

The same principle was recently invoked by the District Court in Massachusetts, Colonial Tavern, Inc. v. Byrne, (In re Colonial Tavern, Inc.), 420 F.Supp. 44 (1976), which noted:

> The force of Judge Hand's opinion [in Bay Ridge] is even more apparent in the context of a Chapter XI proceeding, which

> is voluntary, and in which Rule 11-44 operates automatically upon the filing of a petition. If the debtor's position were to be adopted, Chapter XI would provide an instantly available, cheap and easy sanctuary from all state regulatory enforcement proceedings

-- a consideration equally applicable to a reorganization under Chapter XII. See also In re Shippers Interstate Service, Inc., (Appeal of NLRB), 618 F.2d 9 (7 Cir. 1980); and NLRB v. Jonas, (In re Bel Air Chateau Hospital, Inc., 611 F.2d 1248 (9th Cir. 1979), applying the same rule to labor board proceedings.

Another consideration implicit in this principle is that the Bankruptcy Court, with its paramount concern for the success of the particular reorganization or for maximizing recovery by creditors, may well have little interest in the state's enforcement of its regulatory powers[6] where this endangers the success of the particular

reorganization. The opinion of the bankruptcy judge, here, for example, made repeated reference to three years of effort expended in achieving successful reorganization which would be aborted if the C.O. were revoked.

Judge Galgay recognized the existence of the principle, but, in my view, gave insufficient deference to it. Because he found improper motivation and political influence, he considered this not to be a valid exercise of state police power and therefore not within the rule of the Bay Ridge case. The conclusion does not follow. This reasoning effectively gives the Bankruptcy Court supervisory review of state regulations.

The authority of the New York City Department of Buildings and of the Board of Standards and Appeals over zoning is a matter of state regulatory power, outside the scope of the

exclusive jurisdiction of the Bankruptcy Court. If those regulatory agencies act in a discriminatory and improperly motivated fashion, redress lies in the state courts according to the review provisions of state law.[7] The arguments advanced by the trustee that state review is too slow to save the reorganization are irrrelevant. The exclusive jurisdiction and automatic stay provisions were never intended to place a bankrupt above and beyond the reaches of state regulatory law.

The order appealed from is reversed and the case remanded.

SO ORDERED :

Dated: New York, New York
February 25, 1981

PIERRE N. LEVAL
U.S.D.J.

Footnotes

1. Case No. 77 B 2265.

2. The City's claim is that, although the nursing home was in accord with the applicable zoning regulations when built, later amendments to the zoning regulations made the use of the building as a nursing home a non-conforming use; its authorization for non-conforming use had been abandoned through non-use and was therefore subject to revocation.

The trustee argues that the City's interpretation of the applicable zoning regulations is inaccurate on a number of grounds; first, the trustee claims that the zoning amendments were not meant to apply to buildings that were already constructed; second, even if the amendments did apply to such buildings and the use of the buildings as a nursing home was a non-conforming use, the building had never been abandoned, and thus, the non-conforming use had not lapsed. Because I do not think that the Bankruptcy Court is an appropriate forum for the determination of the correct interpretation and applicability of the zoning regulations I do not reach the merits of the zoning dispute; I note that the dispute appears to involve at least one question of first impression under New York State law.

3. The trustee sought in the alternative that Goldstein be held in contempt for violation of the automatic stay of Rule 12-43, which application was denied.

4. It is worth noting that in the area of zoning and land use planning federal courts have often abstained in deference to the primacy of local governmental policy. See, e.g., Isthmus Landowners Ass'n. v. California, 601 F. 2d 1087 (9 Cir. 1979); Ranchos Palos Verdes Corp. v. City of Laguna Beach, 547 F. 2d 1092 (9 Cir. 1976); Hill v. El Paso, 437 F.2d. 352 (5 Cir. 1971).

5. The new Bankruptcy Code, which does not apply to this case, explicitly provides that the automatic stay provision does not operate as a stay

> of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power.

[Presently enacted as 11 U.S.C. § 362(b) (4).]

6. See, e.g., In re Zeitzer Food Comp., 9 C.B.C. 414 (E.D.N.Y. 1976) (state enjoined from revoking license to purchase and resell farm products); Whalen v. Parkchester General Hospital, (In re Parkchester General Hospital), 4 B.C.D. 292 (S.D.N.Y. 1978) (automatic stay applies to proceedings to revoke hospital's operating certificate; court vacated stay); Hillsdale Foundry Co. v. People, (In re Hillsdale Foundry Co.), 2 C.B.C. 342 (W.D.Mich. 1974) (automatic stay covers enforcement of air pollution law); compare Diversion-Graphics, Inc.

v. Lefkowitz, (In re Diverse-Graphics, Inc.), 2 B.C.D. 194 (S.D.N.Y. 1976) (automatic stay does not stay state criminal proceedings).

7. Additionally, if constitutional rights are involved, redress may lie in the federal courts under civil rights statutes.

APPENDIX C

Opinion of the Bankruptcy Court

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter of	:	No. 77 B 2265
NATIONAL HOSPITAL AND INSTITUTIONAL BUILDERS COMPANY, a Partnership	:	MEMORANDUM AND ORDER 10/8/80
Debtor.	:	

JOHN J. GALGAY - Bankruptcy Judge

James L. Garrity, as trustee for the National Hospital and Institutional Buildings Company ("Debtor"), asks this Court to rule that the stay imposed by Rule 12-43 of the Rules of Bankruptcy Procedure ("Rule 12-43") bars Philip Goldstein ("Goldstein"), as Borough Superintendent of New York City Department of Building, and the Board of Standards and Appeals, (collectively the "City"), from instituting or continuing proceedings

to revoke the Debtor's Certificate of Occupancy (C.O.). After careful review of the history of this prolonged case and of the policies underlying the role of the automatic stay in a real property arrangement, this Court grants the motion of the trustee.

The Debtor, a New York partnership, is the fee owner of real property in Staten Island improved with an unlicensed, unopened nursing home facility. Approval for the establishment of the home was obtained from the Department of Hospitals of New York City in April 1966, and construction commenced in June 1969. Washington Federal Savings and Loan ("Association") has an outstanding mortgage on the property of approximately $2 million.

On or about June 8, 1978 the Association commenced an action to foreclose its mortgage in the Supreme Court of the State of New York, County

of Richmond. A final judgment of foreclosure and sale was entered on July 1, 1977 and the foreclosure sale was scheduled for September 1, 1977. On August 31, 1977 the Debtor filed a petition for an arrangement pursuant to Chapter XII of the Bankruptcy Act, 11 USC 801-926, and an automatic stay of all suits and lien enforcements was imposed by Rule 12-43.

On October 17, 1977, on application of the Debtor, James L. Garrity was appointed as trustee. This Court directed him to investigate the possible uses of the nursing home facility which would form the basis of the Debtor's plan of arrangement. At that point in time the State of New York contended that the nursing home had not been properly established in 1966. Because of an alleged excess of nursing home beds in Staten Island, the state refused to grant establishment approval for the nursing home.

On March 21, 1978 the trustee and his counsel secured the agreement of the Department of Health of New York State that establishment approval might be granted to the home under the religious group exception to the need requirement of Section 2801-a(3) of the New York Public Health Law. The state indicated that it would entertain an application by an Hassidic group which could satisfy the state as to its bona fides and as to the existence of an unmet need for nursing home facilities among its adherents.

The trustee entered into a contract for sale of the property to Beth Rifka, Inc, an Hassidic organization. A condition precedent to the closing of this transaction was the granting of establishment approval, operating certificate and other such approvals as required by the state for the opening of the nursing home. Beth Rifka

submitted its application for establishment approval to the New York State Department of Health, and after numerous meetings and inquiries the Public Health Council of the State of New York, as final licensing authority, granted the application with certain minor conditions.

During the next several months all the parties worked to obtain satisfactory financing arrangements. The high interest rates prevailing during the winter and spring required an additional approval by the Public Health Council before the financing could be finalized. This final approval was granted on September 19, 1980.

The present controversy concerns the existing Certificate of Occupancy for the premises. A temporary C.O. had been issued by the city on January 10, 1973 and a final C.O. for a 240

bed nursing home W24 [sic] accessory parking spaces was issued on June 11, 1973.

By a letter dated May 7, 1980, Goldstein threatened to institute proceedings before the New York City Board of Standards and Appeals to revoke the C.O. The letter stated that under applicable regulations the Debtor's use of the facility was a non-conforming use which had been discontinued and could therefore not be resumed. On June 11, 1980, counsel to the trustee advised Goldstein that the Department of Buildings is stayed pursuant to Rule 12-43 from prosecuting any appeal to the Board of Standards and Appeals to revoke the C.O. Subsequently Goldstein advised the trustee's counsel of his intention to institute the proceedings on the advice of his own counsel that the automatic stay was inapplicable.

The Debtor's building has been vacant since its completion while avenues to open it as a nursing home have been pursued. Prior to the filing of the Chapter XII petition and throughout the lengthy proceedings and hearings before the administrative agencies and departments which had to rule on Beth Rifka's application, Goldstein and the Bureau [sic] of Standards and Appeals took no action to revoke the C.O. The Debtor has proceeded with its plans to finally open the nursing home, and all of the parties have expended a great deal of time and energy in bringing that plan to fruition.

From the record, it appears that Goldstein's action may have been initiated after certain community groups opposed to the nursing home cited some zoning regulations under which the use of the property as a nursing home may be non-conforming in that district. Goldstein's

letter of June 30, 1980 to New York City Commissioner Irwin Fructman [sic] stated that various Staten Island residents had requested that the Department of Buildings apply to the Board of Standards and Appeals for revocation of the C.O.

By a letter dated August 4, 1980, without leave of this Court, Goldstein applied to the Board of Standards and Appeals for such revocation. An affidavit submitted by the Office of General Counsel to the Department of Buildings of the City of New York stated that "under zoning resolutions §§22-13, 74-90 and 74-903, the nursing home use i[s] a non-conforming use which is lost by non-use of two or more years unless a Special Permit is obtained from the City Planning Commission or a variance is obtained from the Board of Standards and Appeals. The Trustee may pursue his remedies to obtain a Special Permit or

variance. The Department will not oppose such application of the Trustee." (Emphasis added). This affidavit clearly indicates that the Department of Buildings does not contend that the facility somehow endangers the local community, is unsafe to its proposed occupants or will have a deleterious effect on the neighborhood. The Court takes notice of the fact, as reported by the Trustee, that the nursing home is located between a hospital and a medical center.

It is against this background of three years of work by the parties to rehabilitate the Debtor within this Chapter XII proceeding that the present action by Goldstein must be viewed. Section 411 of the Bankruptcy Act, 11 USC 811, grants the court in which the Chapter XII petition is filed "exclusive jurisdiction over the debtor and his property,

wherever located." From this express grant of jurisdiction flow the broad injunctive powers which the court can exercise to preserve that exclusive jurisdiction. See Rules Comment to §411.

Although the Bankruptcy Act contains no exact definition of what constitutes the property of a debtor, the courts have clearly found that operating licenses integral to a reorganizational proceeding are property subject to the jurisdiction of the Bankruptcy Court. See Carolina Pipeline Company v. New York County Natural Gas Authority, 388 F.2d 297 (4th Cir. 1967); In re Zeitzer Food Corp, 9 CBC 614 (E.D.N.Y. 1976); In re Parkchester General Hospital 4 Bankr. Ct. Dec. 292 (S.D.N.Y. 1978). It follows that the C.O. which Goldstein seeks to have revoked is property of the Debtor. The nursing home facility is the Debtor's sole

asset. Revocation of the C.O. will significantly impair the value of the asset and completely undermine any rehabilitation of the Debtor.

In In re Zeitzer, supra, the court determined that the automatic stay of Rule 11-44 (a) of the Rules of Bankruptcy Procedure is applicable to administrative proceedings to revoke an operating license of a debtor, absent a showing that there is an encroachment on the police power of the state to protect the health and welfare ofthe community. 9 CBC 624. The language of Rule 12-43 is almost identical to the language of Rule 11-44(a) and the cases decided under the Chapter XI rules are applicable to a Chapter XII proceeding. Similarly, this Court held that an administrative proceeding by the New York State Commissioner of Health to revoke an operating certificate for a debtor's hospital was automatically stayed by the

filing of the Chapter XI petition and required permission of the court, after a showing of good cause, to vacate that stay. In re Parkchester General Hospital, 4 Bankr. Ct. Dec. 292 (S.D.N.Y. 1978). Goldstein has commenced his action against the Debtor while the Debtor and his property are under the protection of this Court and without the showing of good cause which the court would require to vacate the stay under Rule 12-43(d).

In a very recent case decided under the new Bankruptcy Code, the court reviewed the legislative history of the new automatic stay provision and the narrow exception carved out for certain administrative proceedings. The new Code provision reflects the trend under prior case law under the Bankruptcy Act to prevent actions that would result

in the taking of the debtor's property without a Bankruptcy Court order. See 2 Collier on Bankruptcy 362.05 (15 ed.)

> "Section 362(b)(4) indicates that the stay under Section 362(a)(1) does not operate to affect the commencement or continuation of an action or proceeding by a governmental unit to enforce the governmental unit's police or regulatory power. This Section is intended to be given a narrow construction in order to permit governmental units to pursue to protect the health and safety..."

In re King Memorial Hospital Inc, 6 Bankr. Ct. Dec. 634, 635 (S.D. Fla. 1980) quoting 124 Cong Rec H 11089 (Dec. 1978). In that case the court held that any determination by the Department of Health and Rehabilitative Services that the debtor hospital had forfeited its exception from the Certificates of Need Law was enjoined by the

automatic stay as not evidencing an exercise of the police power to protect the public health and safety.

Similarly, this court finds that the action proposed by the City to revoke the C.O. is not within the valid exercise of its police power under the zoning laws. If there was a legitimate concern for the protection of the public health and welfare of the community surrounding the Debtor's property, then an administrative action should have been brought much earlier. The C.O. was issued on June 11, 1973. In all this time the City never sought to revoke or even inquire into the bona fides of the Debtor's C.O. Now, more than three years after the filing of the bankruptcy petition on the eve of consummation of the Debtor's plan, the City has seen fit to

commence revocation proceeding without leave of this Court.

The State of New York, after extended administrative review, has determined that the Hassidic population of New York City has an unmet need for a nursing home which can be appropriately filled by the opening of the Debtor's already constructed facility. The State has also determined that Beth Rifka has the financial resources to successfully operate this facility. The interest of the State in the orderly administration of a health care program for the benefit of the community clearly outweighs the technical objection of the City concerning the trustee's lack of a Special Permit to which the Department of Buildings has no opposition.

The motion of the trustee seeking an order that Goldstein and the Board of Standards and Appeals are stayed from instituting or continuing proceedings to revoke the Debtor's Certificate of Occupancy is hereby granted.

The alternative motion adjudging Goldstein in contempt of the Rule 12-43 automatic stay is hereby denied.

It is so ordered.

Dated: New York, New York
October 8, 1980

Bankruptcy Judge

CIA

Opposition

NO. 81-951

Office - Supreme Court, U.S.
FILED
DEC 21 1981
ALEXANDER L. STEVAS,
CLERK

In the
SUPREME COURT OF THE UNITED STATES
October Term, 1981

In the Matter of National Hospital and Institutional Builders Co.

PHILIP GOLDSTEIN, NEW YORK CITY DEPARTMENT OF BUILDINGS and NEW YORK CITY BOARD OF STANDARDS AND APPEALS,

Petitioners,

v.

JAMES L. GARRITY, Trustee of National Hospital and Institutional Builders Co., Debtor,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals For the Second Circuit

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION

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Counter-Statement of Questions Presented

1. Should certiorari be granted where the issues to be reviewed are insignificant and concern a statute that has been superseded by a different statute?

2. Does the Bankruptcy Court have jurisdiction under the Bankruptcy Act of 1898 to enjoin enforcement of zoning laws where there has been a finding of bad faith enforcement?

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION

Preliminary Statement

The respondent, James L. Garrity, Trustee of National Hospital and Institutional Builders Company, Debtor, respectfully requests that this Court deny the petition for writ of certiorari, seeking review of the Second Circuit's opinion in this case. That opinion is reported at 658 F.2d 39.

James L. Garrity, court-appointed Trustee of National Hospital and Institutional Builders Company, a Chapter XII debtor in possession under the Bankruptcy Act, moved by order to show cause in the Bankruptcy Court to restrain Philip Goldstein as Borough Superintendent of the New York City Department of Buildings, and the Board of Standards and Appeals from instituting or continuing proceedings to revoke a previously granted and long standing

certificate of occupancy for the Debtor's nursing home. After notice and hearing the motion was granted and an injunction issued. On appeal to the District Court the injunction was dissolved. Thereafter, on March 13, 1981 the District Court granted the Trustee's motion for a stay pending appeal.

The Court of Appeals for the Second Circuit thereafter held that an application for revocation of a certificate of occupancy was a proceeding against the debtor controlled by Bankruptcy Rule 12-43 and thus the Bankruptcy Court had jurisdiction to stay the attempted revocation of the Debtor's certificate of occupancy.

COUNTER-STATEMENT OF THE CASE

Since December 1, 1975, the Debtor, a New York partnership, has been the fee owner of real property improved

with a fully equipped nursing home facility. Until recently the nursing home facility stood empty, unopened and unlicensed. On February 16, 1981, after the Trustee advised both the District Court and the Bankruptcy Court, the nursing home, having obtained all the necessary licenses, began admitting residents.

Approval for the establishment of the nursing home (later disavowed) was initially obtained in April, 1966, from the New York City Department of Hospitals. Construction began in June, 1969. Foundation permits were issued on June 17, 1969 and on December 2, 1969. Plans were finally approved on October 20, 1970, and a full permit issued. Temporary certificates of occupancy were issued on January 10, 1973 and March 6, 1973. A final certificate of occupancy for a

240-bed nursing home was issued on June 11, 1973.

Ever since the building which is the subject of the administrative proceedings commenced by the City was completed, and until very recently, it stood vacant while avenues to open it as a nursing home were pursued. Primarily as a result of the State's refusal to grant the needed approval, the Debtor on August 31, 1977 filed a petition for a real property arrangement pursuant to Chapter XII of the Bankruptcy Act. All creditors, including the City of New York, were notified by the Bankruptcy Court of the filing of the petition.

In March, 1978, the Trustee finally secured the agreement of the New York State Department of Health that establishment approval could be granted to the nursing home under the religious group exception to the need requirement

of Section 2801-a(3) of the New York Public Health Law.* The State indicated that it was prepared to establish an Hassidic group which could satisfy the State as to its bona fides and as to the existence of an unmet need for nursing home facilities among its adherents.

Thereupon, the Trustee entered into negotiations with the prospective purchaser and, on July 18, 1978, executed a contract with Beth Rifka, Inc. ("Beth Rifka"), an Hassidic Jewish group, for the sale of the property as a nursing

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* Ordinarily, an application for establishment will not be approved unless the applicant satisfies the State that (a) there is a public need for the existence of the nursing home at the time and place and under the circumstances proposed; (b) the proposed operators of the nursing home are of good character, competence and standing in the community; and (c) the applicant has adequate financial resources to operate the nursing home. The "public need" requirement is waived where the nursing home is to be operated by a religious organization. The needs of the members of the religious denomination for the care or treatment of their adherents are deemed to be public need.

home. A condition precedent to the closing of this transaction was the granting of establishment and various other State and federal approvals. A short time later, on August 3, 1978, Beth Rifka submitted to the Department of Health its application for establishment approval pursuant to the religious exemption provision of State law.

After the Trustee, the Debtor and Beth Rifka had met numerous times with and had fielded numerous inquiries by and from the various health care deliberative and determinative bodies, on August 24, 1979, the Public Health Council of the State of New York, the final licensing authority, approved Beth Rifka's application for establishment approval for the nursing home subject to certain minor conditions. This approval was granted despite vigorous opposition mounted by members of the local community.

Because of certain improper procedures on its own part, the Public Health Council afterwards rescinded its approval and resubmitted the application, which was again approved with minor conditions on December 21, 1979.

During the next several months, all of the parties worked to obtain satisfactory financing arrangements and eventually came to an accord. Unfortunately, the high interest rates prevailing during the winter and spring of 1980 required an additional approval by the Public Health Council before the financing could be effected. This final approval was obtained in December, 1980, subject to certain minor conditions. The way was now clear for the sale to Beth Rifka to be consummated, thus providing the economic basis to confirm the Chapter XII plan of arrangement.

Prior to the filing of the Chapter XII petition and throughout the protracted proceedings and hearings before the various administrative agencies and departments which had to rule on Beth Rifka's application, the City sat by silently, allowing the Debtor to proceed with its plans to finally open the nursing home. Bowing eventually to pressure from politically prominent Staten Island residents opposed to the operation in their neighborhood of a nursing home with facilities to serve the needs of Hassidic News, the City Department of Buildings threatened to institute proceedings before Standards and Appeals to revoke the nursing home's certificate of occupancy. This belated threat was contained in a letter from Goldstein dated May 7, 1980 (seven years after the issuance of the Certificate of Occupancy) in which he stated that under

applicable regulations, the Debtor's use of the facility was a non-conforming use which had been discontinued and could therefore not be resumed. Carbon copies of this letter were sent to, among others, the local Staten Island Civic Association and the Borough President, establishing clearly the motivating force behind the City's sudden and belated action.

On June 11, 1980, the Trustee's special counsel advised Goldstein by letter that the Department of Buildings was stayed pursuant to Rule 12-43 of the Federal Rules of Bankruptcy Procedure from prosecuting any proceeding to Standards and Appeals to revoke the Certificate of Occupancy.

On June 30, 1980, Goldstein wrote to Commissioner Irwin Fruchtman that various Staten Island residents had requested the Department of Buildings to

apply to Standards and Appeals for revocation of the certificate of occupancy. Goldstein stated that he had "received [such] a letter from Mr. Bruce G. Behrins, an attorney for the Concord Civic Association, the Dongan Hills Estates Civic Association and the Grasmere Civic Association." He stated further that he had "also received inquiries" about the nursing home "from Lillian Prado, District Manager of Community Board No. 2 and from the Borough President's office." Goldstein recited that the arguments to be advanced in support of revocation had been set forth by Mr. Behrins. Goldstein acknowledged in his letter that he had been informed by the Trustee's counsel that the contemplated proceeding to revoke the certificate of occupancy contravened the automatic stay of Rule 12-43. Carbon copies of this letter were sent to, among others, Mr. Behrins,

Borough President Gaeta and Community Board District Manager Prado.

Despite the communications which he received from the Trustee's general and special counsel, Goldstein, without leave of the Bankruptcy Court, by letter dated August 4, 1980 applied to Standards and Appeals "for revocation of the certificate of occupancy of the Danube Nursing Home at 1000 Targee Street."* This application laid out the arguments for revocation advanced by Mr. Behrins. It is the proceeding commenced by this application which the Bankruptcy Court determined was violative of the automatic stay and could not be allowed to proceed, which decision was reversed by the District Court and subsequently upheld by the Court of Appeals.

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* Staten Island locals referred to the then never-opened building as the "Danube Nursing Home."

DECISION OF THE BANKRUPTCY COURT

By Order to Show Cause dated August 7, 1980, the Trustee moved the Bankruptcy Court for an order staying Goldstein and Standards and Appeals from instituting or continuing proceedings to revoke the Debtor's certificate of occupancy or, in the alternative, adjudging Goldstein in contempt of the automatic stay imposed by Rule 12-43 of the Federal Rules of Bankruptcy Procedure and certifying the facts constituting such contempt to the district court. Because of the agreement of the parties as to the material facts, the Bankruptcy Court did not take testimony but invited the parties to submit proposed findings of fact and conclusions of law. By memorandum and order entered October 8, 1980, the Bankruptcy Court granted the Trustee's motion for injunctive relief

and denied the alternative relief which he had requested. The Bankruptcy Court held that the certificate of occupancy was property of the estate which the Court had the jurisdiction to protect in order to prevent the collapse of this Debtor's significant rehabilitative efforts.* The Court also held that whereas under the Bankruptcy Act it may be appropriate for a stay to be lifted upon a showing that there would otherwise be an encroachment on the legitimate police power of a governmental unit, here, there was no such showing because (1) the City's actions appeared to be politically motivated and based on a

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* The Bankruptcy Court also held that the City's action was procedurally defective in that it should not have proceeded unilaterally but, rather, should have proceeded under Bankruptcy Rule 12-43(d) to lift the stay. However, the finding of improper motivation on the City's part would operate to bar relief under Rule 12-43(d) even if the proper procedure had been followed.

legal technicality rather than being inspired by any concern for health, safety or welfare and (2) the State, whose interests in the care of its elderly was paramount to the City's assertion of technical objections under the zoning law, had determined that the Hassidic Jewish population had an unmet need for nursing home beds which could be satisfied by this already constructed facility (at a cost to the public far less than the cost of constructing a new facility*). In view of these findings and its determination that revocation of the certificate of occupancy would "significantly impair the value of the asset and completely undermine any

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* By virtue of the federal and State Medicaid and Medicare reimbursement schemes, the cost of acquiring or constructing a nursing home is borne primarily by various governmental authorities. Ultimately, therefore, the public pays for these facilities.

rehabilitation of the Debtor," the Bankruptcy Court declined to permit continuation of the proceedings commenced in derogation of the stay, holding that it had the jurisdiction to do so both by virtue of the automatic stay and its inherent injunctive power.

DECISION OF THE DISTRICT COURT

The City appealed the order of the Bankruptcy Court to the District Court. Several civic associations sought to intervene as amicus curiae before the District Court but their motion to intervene was denied on March 2, 1981. By an opinion and order dated February 25, 1981, the District Court (Leval, J.) reversed the case and remanded the case to the Bankruptcy Court. The District Court's view of the law was diametrically opposed to the view held by the Bankruptcy Court. Both Courts

acknowledge that the basic facts are not in dispute and differ solely on their interpretation of the law. The essence of the difference of opinion between the District Court and the Bankruptcy Court was the opinion of the former that the latter ". . . failed to give proper deference to the rule that state regulatory power is beyond the scope of Section 411's exclusive grant of jurisdiction." The District Court contrasted the responsibility and expertise of state agencies in establishing and enforcing their statutory mandate in a uniform fashion with the responsibility and expertise of the Bankruptcy Court to achieve orderly reorganization or distribution to creditors. The District Court held that the Bankruptcy Court's responsibility is not infringed if the bankrupt remained subject to local regulatory power and that, in all events, the bankruptcy

court is devoid of jurisdiction to interfere with the exercise of that power. Relying primarily on Smith v. New York State Liquor Authority (In Re Bay Ridge Inn, Inc.), 94 F.2d 555 (2d Cir. 1938) and its progeny, the District Court held fast to the proposition that the jurisdiction of a Bankruptcy Court does not extend to the enforcement of state regulatory power. The District Court ignored the uncontested fact that the certificate of occupancy is "property" of the bankrupt estate and dismissed as irrelevant the findings of the Bankruptcy Court of improper motivation and political influence as a basis for an exemption to the general rule established in Bay Ridge. By so doing, the District Court also rejected the cases relied upon by the Trustee which gave rise to an exception to the general rule of federal abstention as employed in Bay Ridge. The District

Court's decision precluded the Bankruptcy Court from determining, in the first instance, whether it has jurisdiction, i.e., that the purported exercise of the police powers was in bad faith and lacked bona fides.

DECISIONS OF THE SECOND CIRCUIT

On appeal by the Trustee, the Court of Appeals for the Second Circuit upheld the Bankruptcy Court's power to impose an order staying the enforcement of the revocation proceedings by Goldstein and Standards and Appeals. The Court held that Bankruptcy Rule 12-43, which was in effect at the time the debtor filed its Chapter XII petition, was broad enough to empower the Bankruptcy Court to stay the City's intended revocation of the Debtor's certificate of occupancy. The Court reasoned that an application for revocation is no less a

"proceeding against the debtor" under Rule 12-43 than a court proceeding or a pending arbitration in light of the importance of the certificate of occupancy and the substantial weight accorded it by the City.

The Court further held that there must be a finding of bad faith on the part of the City regarding the proposed revocation before it could be determined whether the City was entitled to relief from the automatic stay. Significantly, the Court expressly rejected the City's argument that the new Bankruptcy Code dictated that a stay was impermissible because it specifies that the automatic stay does not apply to proceedings by governmental units to enforce their police or regulatory powers. It stated that the Bankruptcy Act, not the new Code, controlled, that the new Code's stay provision "provides

little direction for interpreting the stay under the Act," and that "Congress removed local regulation only from the effect of the automatic stay; it did not eliminate the Bankruptcy Court's power to enjoin the enforcement of local regulation which is shown to be used in bad faith." 658 F.2d at 43.

REASONS FOR NOT GRANTING THE WRIT

1. The Second Circuit's Holding That The Bankruptcy Court Has Jurisdiction Under The Bankruptcy Act To Enjoin A City From Enforcing Its Zoning Laws Where There Is A Finding Of "Bad Faith" Enforcement Raises No Significant Question To Be Reviewed In This Court

This case raises not one important question warranting this Court's review of the decision of the

Second Circuit.* Whether the automatic stay provision of the Bankruptcy Act of 1898 is applicable to "bad faith" matters of police and regulatory enforcement is not an issue of sufficient significance necessitating this Court's review. Nor is the issue as to whether a certificate of occupancy is "property" of the debtor within the exclusive jurisdiction of the Bankruptcy Court under Section 411 of the Bankruptcy Act one important enough to merit this Court's intervention.

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* Even assuming, as petitioners claim, that the courts are in conflict regarding the applicability of the automatic stay to matters of police and regulatory enforcement, such a conflict alone is not enough to justify granting certiorari. The conflict must, of course, concern a significant issue. See New Rider v. Board of Education of School District No. 1, 414 U.S. 1097 (1973), Freeman v. Flake, 405 U.S. 1032 (1972), Olff v. East Side Union High School District, 404 U.S. 1042 (1972), in each of which this Court denied certiorari even though eight circuits had divided equally on the recurring issue as to whether local school boards can regulate the length of students' hair. Freeman, supra, 405 U.S. at 1292 (Douglas, J., dissenting).

Furthermore, whatever the significance of the legal issues in this action, they are governed by the Bankruptcy Act of 1898 which has been superseded by the new Bankruptcy Code and therefore apply at most to a mere handful of actions still pending under the Bankruptcy Act. There is, therefore, little point to this Court's reviewing what has become, in essence, a moot question.

According to Mr. Justice Harlan, "even where a 'true' conflict may be said to exist, certiorari will sometimes be denied where it seems likely that the conflict may be resolved as a result of future cases in the Court of Appeals, or where the impact of the conflict is narrowly confined and is not apt to have continuing future consequences, as where a statute which has given rise to conflicting interpretations

has been repealed or is about to expire." Mr. Justice Harlan, "Some Aspects of the Judicial Process in the Supreme Court of the United States," 33 Australian L.J. 108 (1959) (emphasis added).

This Court has denied certiorari even where there has been a real conflict in cases where the statute upon which the controversy rested had expired or had been amended in a manner which prevented the problem from occurring in the future. See, e.g., United States v. Abrams, 344 U.S. 855 (1952); Community Services, Inc. v. United States, 342 U.S. 932 (1952); Sokol Bros. Furniture Co. v. Commissioner of Internal Revenue, 340 U.S. 952 (1951); Beal v. United States, 340 U.S. 852 (1950); United States v. Wilkinson, 355 U.S. 839 (1957), as described in Berger v. United States, 170 F.Supp. 795 (S.D.N.Y.

1959); United States Rubber Co. v. Commissioner, 363 U.S. 827 (1960).

In addition to the insignificance and mootness of the legal questions at issue here, the "conflict" pointed to by petitioners as justifying this Court's issuing a writ is illusory.

This Court's holding in Palmer v. Massachusetts, 308 U.S. 79 (1939) to the effect that a Bankruptcy Court cannot usurp the functions of a State railroad commission and permit a railroad in reorganization to abandon local service does not conflict with the Second Circuit's decision in this case and accordingly is not a reason for granting the writ. The Palmer holding is grounded upon the fact that the debtor there was a bankrupt railroad. This Court specifically stated that "the whole scheme of § 77 [that part of the Bankruptcy Act pertaining to railroad

reorganizations] leaves no doubt that Congress did not mean to grant to the district courts the same scope as to bankrupt roads that they may have in dealing with other bankrupt estates." 308 U.S. at 87.

Even assuming that Palmer is in conflict with the Second Circuit's decision herein, that in itself is an insufficient ground for certiorari to issue, for, as noted by Messrs. Stern and Gressman, "it is to be doubted that a contrary opinion rendered 30 or 40 years ago, without any indication that it has current vitality, will be enough to convince the Court that there is a live conflict which should be resolved." Stern and Gressman, Supreme Court Practice, p. 271 (5th Ed. 1978).

Furthermore, In re State of Missouri, 647 F.2d 768 (8th Cir. 1981) is not apposite to this case because

there the Court stated in dictum only that automatic stays under the Bankruptcy Act "did not apply generally to proceedings affecting the public health and safety or certain regulatory activity." The bankruptcy petition in that action was filed in 1980 and hence was governed by the new Bankruptcy Code which specifies in § 362(b)(4) that the automatic stay does not apply to proceedings by a governmental unit to enforce its police or regulatory powers. Moreover, the Court actually held that the automatic stay was proper because the Missouri grain laws at issue primarily related not to matters of safety and health but to the protection of the pecuniary interest in the debtors' property. 647 F.2d at 776.*

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* Similarly, State of Ohio v. Mansfield Tire and Rubber Co., 660 F.2d 1108 (6th Cir. 1981) is not relevant to this case because it too was governed by the new Bankruptcy Code and § 362(b)(4).

Moreover, the alleged conflict of the Second Circuit's holding in this case with the "numerous authorities" cited in In re State of Missouri, supra, 647 F.2d at 775, is irrelevant as to whether certiorari should issue here. Most of those decisions, even if truly in conflict with the Second Circuit's holding here, were rendered by bankruptcy and district courts, and this Court will not grant certiorari to review a decision of a federal court of appeals merely because it directly conflicts with a district court decision. Stern and Gressman, Supreme Court Practice, p. 278 (5th Ed. 1978).

2. The Second Circuit's Holding That The Bankruptcy Court Has Jurisdiction Under The Bankruptcy Act To Enjoin Enforcement Of Zoning Laws Where There Is A Finding Of "Bad Faith" Enforcement Is Correct

The Second Circuit was correct in its determination that the Bankruptcy Court possesses the power to examine the bona fides of administrative action, taken under color of the police power, in order to determine its jurisdiction to protect property of the Debtor's estate.

The Court of Appeals properly interpreted Bankruptcy Rule 12-43, which provides that the petition "shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor . . . or of any court proceedings to enforce any lien against his property" as being broad enough to stay the City's intended

revocation of the Debtor's certificate of occupancy. The Court concluded that "[g]iven the importance of the C.O. to the Debtor and the substantial weight the C.O. is accorded by the City, we cannot say that Goldstein's application for revocation is any less a 'proceeding against the debtor' than a court proceeding or a pending arbitration." 658 F.2d at 42.

As noted by the Second Circuit, if the Bankruptcy Courts lacked the power to protect a debtor's assets from bad faith zoning regulation, "a city interested in the outcome of a bankruptcy petition could seriously interfere with management of the bankrupt estate through repeated threats of harmful zoning." Id. at 43. Obviously, this will wreak havoc with the rehabilitative purpose of Chapter XII.

Conclusion

For all of the foregoing reasons, the petition for a writ of certiorari should be denied, and the Second Circuit's reversal of the District Court's judgment should be allowed to stand in all respects.

Respectfully submitted,

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Petitioner's Reply Brief

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NO: 81-951
IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

IN THE MATTER OF NATIONAL HOSPITAL AND INSTITUTIONAL BUILDERS CO.

PHILIP GOLDSTEIN, NEW YORK CITY DEPARTMENT OF BUILDINGS AND NEW YORK CITY BOARD OF STANDARDS AND APPEALS,

Petitioners,

v.

JAMES L. GARRITY, Trustee of Debtor,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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PETITIONER'S REPLY BRIEF

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PETITIONER'S REPLY BRIEF

Under Rule 22.5 of the Rules of this Court, a reply brief may be filed by a petitioner if the Respondent's Brief in Opposition raises a new argument not covered in the Petition. Since respondent raises the question of whether the issues involved are "significant" enough for this Court to consider, a short reply is being submitted.

The critical question raised by the petition was not limited to the automatic stay of Bankruptcy Rule 12-43 which was superseded by Sec. 362 of the new Bankruptcy Code, insofar as bankruptcies filed on and after October 1, 1979 are involved. As the petition phrases the very first question, the issue is the subject matter jurisdiction of bankruptcy courts to enjoin the exercise of police power under any circumstances. The issue is the same for

matters arising under the Act or under the Code, since lack of jurisdiction does not only limit automatic stays but also affects specific stays or injunctions against the exercise of police powers issued at the behest of a trustee or debtor. As in the Missouri petition (No. 81-79 Oct. 1981 Term), the issue is not merely whether Bankruptcy Rule 12-43 was intended to cover police and governmental regulatory enforcement, but whether Congress ever granted jurisdiction in Secs. 1 or 411 of the Bankruptcy Act or in Sec. 105 of the Bankruptcy Code to permit bankruptcy courts to interfere with state governmental operations. We submit that, by enacting 28 U.S.C. § 1478, barring removal of a civil action by a governmental unit to enforce its police and regulatory powers, Congress declared its intention that bankruptcy courts

should not be involved in this area and limited their authority to directly affect a municipality's exercise of its police power.

CONCLUSION

For the reasons set forth in the petition and in this Brief, the writ of certiorari should be granted.

Respectfully submitted,

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